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Update: New York Legislature Enacts Additional Publication Requirements for Limited Liability Companies and Limited Partnerships

On February 3, 2006, Governor George Pataki signed into law Senate Bill No. 85-A (the "New Law") which amends the publication requirements applicable to foreign and domestic limited liability companies, professional service limited liability companies, limited partnerships and limited liability partnerships. The New Law will be effective on June 1, 2006, but is currently the subject of an important proposed amendment introduced in the New York State Legislature on February 28, 2006 (the "Proposed Amendment").

New Law. The most significant changes effected by the New Law are:

- Additional publication requirements, including a requirement to publish the names of the top ten persons actively engaged in the conduct of the business and having the most valuable ownership interests in the entities (the "top ten requirement"); and

- A more robust sanction for non-publication - suspension of authority to carry on, conduct or transact any business in New York State.

Proposed Amendment. The most significant changes to the New Law that would be effected by the Proposed Amendment are:

- Removal of the top ten requirement enacted by the New Law; and

- Replacement of the New Law's "suspension of authority to do business" sanction by the much more severe sanction of stripping away the protection of limited liability from members or limited partners of the affected entities and making them personally and fully liable, jointly and severally, with such entities and with each other, for all debts, obligations and liabilities of such entities.

This Memorandum discusses both the New Law and the Proposed Amendment in further detail.

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Entities Affected by the New Law

The New Law affects both domestic and foreign limited liability companies, professional service limited liability companies, limited partnerships and limited liability partnerships, that are doing business in New York State.

Investment advisers (as defined in the Investment Advisers Act of 1940), commodity pool operators and commodity trading advisors (each as defined in the Commodity Exchange Act), and any collective investment vehicle or any direct or indirect subsidiary or affiliate sponsored, advised or managed by an investment adviser, commodity pool operator or commodity trading advisor are exempt from the requirement of disclosing a list of their top ten interest holders. It should be noted, however, that these entities are still subject to the publication requirement (without the top ten requirement) and suspension of business sanction for failure to publish, as will be explained below. Theatrical production companies are entirely exempt from the publication requirements.

The Publication Requirements

The New Law expands the previous requirement of publishing information about the entity (such as name of the entity, its address and designation of the New York Secretary of State as agent for service of process, etc.). Publication must be made within 120 days of the entities' formation (foreign entities are required to publish within 120 days of filing an application to do business in New York State). Entities will now be required to disclose the names of the top ten persons actively engaged in the business who have the most valuable membership or partnership interests in such entities. In addition, the New Law requires the publication to include a disclaimer, stating that:

> "The inclusion of the name of a person in this notice does not necessarily indicate that such person is personally liable for the debts, obligations or liabilities of the [entity] and such person's liability, if any, under applicable law is neither increased nor decreased by reason of this notice".

The New Law also reduces the publication requirement of publishing in two newspapers to four successive weeks (from the previously required six successive weeks).

If any of the information in the notice (including the list of the top ten interest holders) changes after completion of the first weekly publication, no further or amended publication will be required. This seems to allow for the use of holding companies or shelf companies which can, after publication, change their ownership interests without having to make this change public.

After publication is made, a publisher's affidavit must be filed with the Department of State, containing the text of the publication as an annex. Previously, the required affidavit did not have to include the actual published text, only proof of publication.

Entities formed prior to June 1, 2006 that had filed at least one publisher's affidavit prior to that date, are not required to make an additional publication under the New Law. Entities formed prior to January 1, 1999 are deemed in compliance without regard to whether the entity filed a publisher's affidavit with the Department of State.

Entities formed between January 1, 1999 and June 1, 2006 that did not comply with the publication requirements of the previous law are granted a "grace period" of 18 months starting June 1, 2006, in which to make the publication as was required under the law prior to June 1, 2006. This means that all such previously formed entities that are not in compliance with the pre June 1, 2006 publication requirement will have 18 months in which to publish without disclosing the identities of the top ten interest holders.

The Sanction for Failure to Publish – Suspension of Authority

An important change in the law is the new sanction for failure to publish. Previously, the statutory penalty for failure to publish was prohibition from maintaining any action or special proceeding in New York State. Under the New Law the penalty for failure to publish is more severe: a suspension of the authority of the business entity to carry on, conduct or transact any business in New York State.

The exact scope and practical effect of this new penalty is unclear, as the penalty is not defined in the statute nor is there any case law on point. The statute does state that neither the failure of the entity to publish nor its suspension due to such failure will limit or impair the validity of any contract or act of such entity or any right or remedy of any other party under or by virtue of any contract, act or omission of such entity (this language is not new and exists in the current statute as well). This would seem to indicate that the penalty for failure to publish under the New Law while harsher than the previous inability to bring a claim, does not amount to a complete inability of the entity to act or conduct its business.

Ability to Cure – Annulment of the Suspension

An entity may, at any time, cure its failure to publish simply by complying with the statute and publishing as required under the New Law. Once the entity has complied, the suspension is "annulled". It is unclear whether this cure is retroactive, although the language seems to indicate so. The statute does not define or explain what the meaning of "annulment" is in this context.

The Proposed Amendment

The Proposed Amendment rolls back some of the changes made by the New Law, including removal of the top ten requirement as well as reverting the newspaper publication

requirement to six successive weeks instead of four. It also reduces the 18 months "grace period" allowed under the New Law to 120 days.

Importantly, the sanction for failure to publish in the Proposed Amendment goes much further than the New Law. Instead of a suspension of authority to do business, the Proposed Amendment strips away the protection of limited liability from members or limited partners:

> "each [member/limited partner] of such [entity] shall be personally and fully liable, jointly and severally with such [entity] and with each other [member/limited partner], if any, of such [entity], for all debts, obligations and liabilities of such [entity] incurred or arising at any time before or after such failure."

The penalty is draconian. However, it is not clear how it would affect foreign entities that were not formed under New York law and therefore may not be controlled by New York law on issues of corporate law, such as limited liability.

The Proposed Amendment does allow for cure of this severe penalty by complying with the publication requirement. However, the language used is vague and it remains unclear whether the cure would be retroactive. It is also possible that the path to cure may not always be clear – for example when an entity has filed for bankruptcy.

The Proposed Amendment, if enacted, would be a powerful deterrent to any person who wishes to conduct business in New York State through one of the business entities referred to in this Memorandum, each of which currently offers its owners the ability to conduct business in New York with limited liability protection.

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This Memorandum is not intended to provide legal advice with respect to any particular situation and no legal or business decision should be based solely on its content. Questions concerning issues addressed in this Memorandum should be directed to any member of the Paul Weiss Corporate Department, including:

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